

## NEW ZEALAND ECONOMICS RBNZ OCR PREVIEW

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## BALANCED AND MEASURED

### KEY POINTS

- **The OCR is biased lower, but like the consensus and market, we don't expect action at the OCR Review on Thursday.** Further easing will be signalled – the NZD is too deflationary to ignore, and doing nothing would send it further skyward – but the RBNZ has shown a preference to move on *Monetary Policy Statement* dates.
- **The key themes shaping a lower outlook for the OCR are little changed from the August MPS:**
  - **Global fragilities remain.** Economic growth is lacklustre, inflation is low and financial markets are still somewhat addicted to central bank liquidity. The debate over Fed policy rages on (still), and while some central banks (ECB & BoJ) are showing a little more hesitancy to ease again, they are not signalling a reversal. **That buoys the NZD. Our currency divergence / rates convergence theme still applies.**
  - **The NZD continues to outperform.** It is just below 78 on a TWI basis and threatening to test parity against the AUD. It is also above the RBNZ's alternative *MPS* scenario, which had the OCR heading far lower (to circa 1%). That said, with domestic growth and commodity prices stronger, some of this NZD strength is not entirely unjustified.
  - **Inflation and inflation expectations are low.** The RBNZ has shown itself to be particularly sensitive to the latter, and some surveyed measures have dipped a tad of late. The strong NZD will mechanically lower the RBNZ's near-term CPI forecasts further. That said, the latest food and petrol price figures have actually seen us lift our expectations for Q3 CPI to +0.1% q/q, which is back in line with the RBNZ's pick.
- **Offsetting themes certainly exist:**
  - **Housing risks remain.** Some anecdotes suggest the latest LVR restrictions have taken a bite out of activity, but it is certainly far too early to say with confidence that they are having the desired impact.
  - **The economy looks a tad stronger than the RBNZ was assuming in July, particularly the labour market and receding dairy sector risks** – whole milk powder prices are up 34% since late July.
- **We remain in an environment where conventional policy signals (growth, output gap, housing, capacity) are flagging no change (or hike!), but they are going head-to-head with factors that are by-and-large beyond the RBNZ's control (global scene, NZD) amidst some concerns over consistently low inflation influencing price-setting behaviour.**
- **The environment needs pragmatism, balance and measured messages. We expect further policy easing to be signalled,** leaving the door well and truly open to a November cut. The strong NZD will continue to "make it difficult for the Bank to meet its inflation objective". That highlights the direction of risk for the OCR. We suspect that the ~35bps of additional OCR cuts signalled in the August *MPS* is still more-or-less the RBNZ's base case. And that is broadly consistent with current market pricing.

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